

The Medical Protective Company

Exhibit 2B – Reserve Study

1) **Methodology**

The projections of the standard 18 segments ultimate indemnity losses and allocated loss adjustment expenses begin with the sequential ultimate projections of reported claim counts, paid with indemnity claim counts, loss indemnity, and allocated loss adjustment expense. Projections using the following methods are estimated using data as of September 30th 2008. The following sections identify the methods used for each of the projection categories:

Reported Counts: Ultimate reported claim counts are projected using the following methods: (a) Reported Count Development Method; (b) Closed Count Development Method; (c) Reported Count Additive Method; (d) Bornhuetter-Ferguson Method; and (e) Reported Count Frequency Method.

Paid Counts: Ultimate paid claim counts are projected using the following methods: (a) Paid Count Development Method; (b) Incurred Count Development Method; (c) Paid Count Bornhuetter-Ferguson Method; (d) Paid to Closed Method; (e) Paid Trended Frequency Method.

Indemnity Losses: Ultimate indemnity losses are projected using the following methods: (a) Paid Loss Development Method; (b) Incurred Loss Development Method; (c) Paid Bornhuetter-Ferguson; (d) Incurred Bornhuetter-Ferguson Method; (e) Hindsight Outstanding Severity Method; (f) Trended Severity Method; (g) Trended Pure Premium Method.

Allocated Loss Adjustment Expenses (ALAE): Ultimate allocated loss adjustment expenses are projected using the following methods: (a) Paid Development Method; (b) Incurred Development Method; (c) Paid Bornhuetter-Ferguson; (d) Incurred Bornhuetter-Ferguson Method; (e) Trended Severity Method; (f) Trended Pure Premium Method (g) Hindsight severity method.

The Medical Protective reserve analysis is composed of 18 standard segments, and 11 nonstandard/miscellaneous segments. Data triangles are available on a quarterly basis. The standard segments are composed of 18 state/region (Fund States vs. MW_ME states etc.) specific and product specific (Claims-made vs. Occurrence) components, and utilize the same templates and methodologies in the projections across all standard segments. Data for the 18 standard segments is organized on an accident year basis for the occurrence product projections, and on a report year basis for the claims-made product projections for Accident/Report years 1993 through 2008. All 18 standard segments exclude Excess of Policy Limits and Excess of Contractual Obligations (XPL/ECO) losses in order to avoid possible distortions in the data per segment. XPL/ECO projections are done separately on a countrywide basis. Mass torts are also excluded in each individual standard segment, as such claims typically have little indemnity liability associated with them, and significantly reduced levels of allocated loss adjustment expenses as compared to non-tort claims. Mass torts

are projected within the miscellaneous section on a countrywide basis. The 18 standard segments represent more than 80% of Medical Protective's total outstanding liabilities. The state grouping for these segments was reviewed as part of the Company's 2008 reserve analysis. New segmentation was chosen that is more homogenous and representative of Medical Protective's writing in various regions of the United States. Each individual segment maintained a level of credibility that allowed adequate analysis of its data while balancing its level of homogenous data. However, new state segmentation will continually be reviewed to ensure homogeneity and segment credibility are properly considered as the company's book of business changes.

Major Segments

The 18 Major (Standard) segments are comprised of the following:

Occurrence:

Fund_States MD-gross
FW_SW_MW MD-gross

INMD-gross
MW_ME MD-gross
OHMD-gross
PAMD-gross
SE_NE MD-gross

TXMD-gross
CWDDS-gross

States Included:

LA, NM, NB, KS
AK, AZ, CA, CO, HI, ID, MT, NV, OR, UT, WA,
WY, AR, OK, MN, ND, SD
Indiana Occ
KY, MI, IA, IL, MO, WI
Ohio Occ
Pennsylvania Occ
AL, FL, GA, MS, NC, SC, TN, VA, CT, DC, DE,
MD, MA, ME, NH, NJ, RI, VT, WV
Texas Occ
Countrywide - DDS

Claims-made:

FLMDC-gross
Fund_States MDC-gross
FW_SW_MW MDC-gross

MW_ME MDC-gross
NCMDC-gross
OHMDC-gross
SE_NE MDC-gross

TXMDC-gross
CWDDSC-gross

States Included:

Florida CM
LA, NM, NB, KS, IN, PA
AK, AZ, CA, CO, HI, ID, MT, NV, OR, UT, WA,
WY, AR, OK, MN, ND, SD
KY, MI, IA, IL, MO, WI
North Carolina CM
Ohio CM
AL, GA, MS, SC, TN, VA, CT, DC, DE, MD, MA,
ME, NH, NJ, RI, VT, WV
Texas CM
Countrywide – DDS

The 11 nonstandard/miscellaneous segments represent categories of liabilities that are unique in nature, and typically require unique or additional methodologies in their projection. The 11 additional segments for Medical Protective include the following: 1) Prior Year Analysis (1958-1992), 2) Death, Disability, and Retirement (DDR), 3) Reporting Endorsements, 4) Hospitals, 5) Spectrum, 6) XPL/ECO, 7) ULAE, 8) Breast Implants, 9) Deductible Credits, 10) Mass Torts, and 11) Phen Fen. Data organization does vary according to each particular segment, but is stratified by report/accident year where appropriate.

2) Adequacy

The following language talks to the adequacy of Medical Protective's reserves as found in the 2009 Actuarial Statement of Opinion signed by James D. Kunce FCAS, MAAA:

"In my opinion, the amounts carried in Exhibit A on account of the items identified:

- A. Meet the requirements of the insurance laws of Indiana.*
- B. Are computed in accordance with accepted actuarial standards and principles.*
- C. Make a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its contracts and agreements.*

Thus, I am making a Determination of Reasonable Provision with respect to the amounts carried in Exhibit A."

The company has reported 1-year adverse development, as measured by Schedule P, Part 2 Summary, in excess of 5% of surplus in calendar years 2002, 2003 and 2004. During these years the company was realizing a shift in the average indemnity amount per paid claim. The increase in accident year severities was seen primarily in the medical malpractice book of business for accident years 1998-2002. In reviewing other medical malpractice carriers' annual statements, it was discovered this phenomenon was seen throughout the entire medical malpractice industry. Factors driving this shift were items such as; larger limits of coverage being purchased by policyholder, increasing jury awards, increased tendency of multiple insureds named on one case as being liable for damages, and change of social attitudes regarding expectations and outcomes of trials.

3) Company Trends vs. Industry Trends

A comparison of industry trends to company trends has not been conducted. As noted above similar adverse development took place in multiple accident years throughout the industry. However, as regards to specific frequency and severity trends no direct comparison to the industry has been preformed.

Exhibit 2B - Surplus Study

1. Provide a general discussion regarding the adequacy of surplus reported on Annual Statement, page 3 (Liabilities, Surplus and Other Funds), line 35, Surplus as regards policyholders, as of the last year-end.

The company's surplus position remains strong with its premium to surplus ratio and reserve to surplus ratios coming in at 54% and 165% respectively. During 2008, the company recorded \$71M in net income, much of which was offset by unrealized and realized losses in the investment portfolio due to the volatile performance in the financial sector during 2008.

No dividends were declared or paid during the year.

NAIC Risk Based Capital ratios reflect strong results for years 2005 through 2008 with adjusted capital in excess of authorized control level 10 times, 9 times, 7 times and 7 times respectively.

The quantitative data supports managements position that surplus is solid.

2. Identify and describe any material events or known material trends, favorable or unfavorable, in the insurer's surplus account in the past five years. This description should include any significant changes in the surplus ratios shown on Exhibit A. If a material unfavorable trend exists, indicate the courses of remedial actions already taken or that are available to the insurer and the effects or potential effects of each.

Material Events:

Unrealized Losses: During 2008, the investment portfolio suffered unrealized losses (net of tax) of \$42M.

Dividends to stockholders: The company paid dividends 2 of the years under review. The company was sold to Columbia Insurance Company, a member of the Berkshire Hathaway group effective July 1, 2005. Prior to that date the company was owned by General Electric Company.

Loss Portfolio Transfer: The company entered into a Loss Portfolio Agreement of reinsurance with its indirect parent Columbia Insurance Company (Columbia) and its affiliate National Indemnity Company (NICO). The transaction was effective December 31, 2005 and under this agreement, Columbia and NICO each assumed 25% of the Company's outstanding net loss and loss adjustment expense reserves at December 31, 2005 equaling \$697M. This transaction effectively cut loss and loss adjustment expense reserves in half.

Changes in non-admitted assets: These variance swings are largely due to changes in the mix of non-admitted premiums receivable or deferred tax non-admitted changes due to loss reserve discounting swings. Additionally, the non-admitted portion of the deferred tax related to the unrealized investment losses are found here.

Material Trends:

The company saw significant premium growth through 2003 and entered into a 25% quota share reinsurance agreement that year. This agreement was renewed for years 2004 and 2005 respectively. Premium in 2008 was flat compared to 2007.

The increase in the reserve to surplus ratio during 2008 was due to the unrealized investment losses during 2008. It has yet to be determined if this is going to be a trend moving forward.

The escalating trend of both the premium to surplus ratio and the reserve to surplus ratio was stopped and reversed in 2005 with the inception of the loss portfolio transfer transaction. As mentioned above, the advent of the 50% quota share transaction will help ensure solid capital ratios moving forward.

Company Defined Items

- 1. For all reports requiring “by county” information, the company may group the data by policy issuing county or other method that is consistent with its ratemaking practices. The company must identify which method is being used. The company must use a consistent method to group the data in all “by county” reports. Data grouped by territory is unacceptable. Describe any changes made to the way in which the data has been grouped during the past ten years and the impact of the change(s) on the reports.**

When data is grouped “by county”, the data is grouped by policy issuing county. No changes have been made in the past ten years with regard to the way data has been grouped.

- 2. Describe any change(s) made to reserving or claim payment practices in the past ten years and the impact of the change(s) on the reports.**

- 3. Define closed claim. i.e., is a claim closed when it is assigned a closed date, or when both indemnity plus expense reserves are \$0, or in some other instance? Describe any change(s) made to this definition in the past ten years and the impact of the change(s) on the reports.**

A claim is considered closed when the indemnity portion is resolved, either a payment is made or the reserve is reduced to \$0. The associated allocated loss adjustment expense (alae) may not be completely resolved at the time the claim is closed, such that the claim may still have some alae reserve and subsequent alae payments before the claim is completely disposed.

- 4. Explain/define the corporate policies written by the company.**

Corporation policies are written for Partnerships and professional Corporations on behalf of physicians insured by Medical Protective (MPCo). The policy covers the corporation for its vicarious liability due to the actions of our insured physicians.

- 5. Each company shall use the base class and territory that is consistent with its most recent rate filing. Please define your**

company's base class and territory. Describe any change(s) made to the base class and/or territory in the past ten years and the impact of the change(s) on the reports.

Exposures are adjusted to base class and territory using the current filed relativities. These relativities have changed during the 10-year experience period, but all years are adjusted with the current relativities so as to be expressed on a common basis.

The base class is 1B and the base territory is 8.

6. Describe any adjustment(s) made to exposures for extended reporting endorsements and the impact of adjustment(s) on the reports.

Extended reporting endorsement (Tail) exposures are included with the Occurrence exposures and are adjusted to an occurrence equivalent basis. The Tail endorsements are adjusted from an individual count to an occurrence exposure basis by determining the report lags represented by each Tail endorsement relative to an Occurrence exposure of 1.0. The report lags are implied from the claims-made step factors and adjusted for inflation.

Each Tail exposure is multiplied by the ratio of the report lags to the corresponding occurrence exposure (1.0). The difference between the retroactive date and the effective date of the endorsement will determine the reporting lags to be included in the calculation of the ratio. The adjusted exposures are multiplied by the filed relativities to develop the base class and territory equivalent exposures.

7. For the maturity year and tail factors disclosure, list each tail factor with the corresponding maturity year if a different tail factor is used for each maturity year. If another method is used, list and describe factors and method used.

The Tail factors used to rate Extended Reporting Endorsements are a function of the time that has elapsed between the retroactive date and the expiration date of the last claims-made policy that corresponds to the effective date of the endorsement. The Extended Reporting Endorsement Factor is a function of the Mature Claims-Made rate. The factors are expressed as follows:

<u>Years Retroactive Date Precedes Expiration Date</u>	<u>Rating Factor</u>
1	.90
2	1.50
3	1.70
4 or more	1.82

8. Define what expenses are included in the expense factor.

Total Fixed Expense includes all operating overhead expenses excluding commissions and premium taxes. This would also include investment expense, but does not include unallocated loss adjustment expenses.

The *Variable Expense Factor* contains a provision for Taxes, Licenses and Fees, a provision for Brokerage and Commissions, and a provision for Underwriting Profit.

- 9. List and define individually any “other” factors used in the rate filing to establish rates. This could include but is not limited to the following: profit load, reinsurance load, investment income, schedule debits/credits, etc.**

Profit load is expressed on an underwriting basis.

Schedule debits/credits represent the average adjustment to manual premiums based on the filed rating rules applicable to the physician classifications.

D,D and R load - Death, Disability and Retirement load.

- 10. Describe any methods and/or assumptions used in creating Reserve Study Exhibit A and why these assumptions are necessary.**

Reconciliation

For this Data Call, MPCo is using the same primary data source used in creating the annual financial statements. Individual records were checked to ensure data is being aggregated correctly per the Data Call instructions.